IMPERIAL TOBACCO COMPANY OF CANADA LIMITED

ANNUAL REPORT 1967

56th Annual Report 1967

Our cover reflects the movement and action of a busy street — and the fast-paced world about us.

Si vous désirez recevoir ce rapport annuel en français, veuillez vous adresser au Secrétaire, case postale 6500, Montréal 3, Qué.

The year at a glance

Imperial Tobacco Company of Canada Limited

CONSOLIDATED NET EARNINGS	
amount for year	$12,741,000
*compared to previous year — increase	279,000
INCOME TAXES	
amount for year	11,592,000
*compared to previous year — increase	278,000
EARNINGS PER COMMON SHARE	
amount for year	1.28
*compared to previous year — increase	.03
INVESTMENTS IN NON-CONSOLIDATED SUBSIDIARIES, INCLUDING LOANS AND ADVANCES	
*amount at beginning of year	13,425,000
increase during year	1,396,000
amount at end of year	14,821,000
RETAINED EARNINGS	
*amount at beginning of year	51,305,000
added during year	5,746,000
amount at end of year	57,051,000
WORKING CAPITAL	
*amount at beginning of year	86,920,000
increase during year	2,743,000
amount at end of year	89,663,000
DIVIDENDS	
amount for year on	
6% cumulative preference shares	366,000
common shares (rate per share 80¢)	7,736,000
all shares	8,102,000

*Compared to 1966 figures revised in accordance with 1967 presentation.

The figures set out on this page provide a quick glance at the results for the year 1967. More comprehensive information appears on pages 17 to 24.

Centennial sentiment was the theme at the Quarter-Century Chapter dinner in Montreal last year. John M. Keith (centre), president of Imperial Tobacco, joined in the fun with members Raymond Leroux, left, and James MacLaughlin who dressed as the two "Old Chums" of pipe tobacco fame. Almost one quarter of all Imperial Tobacco employees now have 25 years or more of service with the Company.

Time of Rapid Change

Behind the scenes of "stable" financial results

The President reports to the Shareholders:

The year 1967 will long be remembered in Canada as the year of Centennial observances, highlighted by Expo in Montreal. On the more sober social, political and economic scene, the year may well be remembered as the watershed of change.

In an earlier era a popular sentiment was that "the more things change, the more they remain the same." It is rather the reverse these days — not only in Canada, but worldwide — "the more things seem to remain the same, the more they change."

So it was in many industrial firms, and in Imperial Tobacco Company of Canada Limited, during 1967. On the surface, business followed its accustomed pattern.

Total consolidated sales of Imperial Tobacco, including wholly-owned subsidiaries, moved upward from $373,069,000 in 1966 to an all-time record of $393,315,000 in 1967. Net earnings increased to $12,741,000 as opposed to a decrease in the previous year. As noted in greater detail on page 17, the consolidated financial statements for 1967 include Beau Chatel Wines Limited for the first time.

Dividends totalled 80 cents per common share, the same as the previous year, and continued to reflect the increased rate introduced in 1965. In the light of the disturbed earning patterns of many companies in Canada last year, Imperial Tobacco's record of uninterrupted dividend payments since 1912 becomes even more notable.

The struggle behind the scenes to achieve at least these results is stern and waged on many fronts; presented in different context, many incidents could be recounted in high drama.

What actually does "time of rapid change" mean? For one thing, and most apparent to the consumer: increases in prices. To meet escalating costs, most cigarette manufacturing companies increased prices on the longer cigarettes — the king size and longer lengths. Additional impact on smokers was the increase announced in the federal mini-budget of November 30 of about 10 per cent on the federal tax of all tobacco products.

As it was, the yield of the federal tax alone from the tobacco industry passed the $500,000,000 mark in 1967 for the first time. The tax burden on smokers is startlingly revealed by these estimated figures for 1967:

On all tobacco products, retail sales value (including taxes) totalled..........	$1,090 million
Of this total, the following was paid in taxes:	
Federal Excise Taxes.........................	$ 505 million
Provincial Taxes................................	$ 85 million

Including the latest increase, cigarette taxes now average 138% of retail selling value (less tax). The Federal Excise Taxes alone are 28 cents on a package of 25 cigarettes. As stated in the annual review of the Canadian tobacco industry for 1967: "The question surely must be: how much "loading" of the tax burden is fair on one segment of the population, and on one segment of industry?"

THE BATTLE FOR PRODUCTIVITY

The sole means of salvation for any company in these times of severe cost-price squeeze is improved productivity. On a total national basis, this is the one brake that can slow down — and, ideally, stop — accelerating inflation.

In Imperial Tobacco the battle for productivity is being waged relentlessly. Testimony to the degree of success is provided in the stable earnings results, but of course in the long term this is not good enough because shareholders eventually will become disenchanted if they see no adequate return for the capital they have invested.

While not too visible to the outside world, sweeping changes were made in the corporate organization of Imperial Tobacco during 1967.

In the Tobacco Operations Group, the two sales companies, Imperial Tobacco Sales and Peter Jackson Sales, were merged into one selling organization with a target of developing new approaches to cover the vast territories that make up Canada. The marketing function has been strengthened by the use of new creative talents and more specialized skills to help embark on new activities.

Among innovations in the Tobacco Operations Group was the creation of a materials management department, which brings together the control of such functions as purchasing, central supply, warehousing, and physical distribution — activities which were previously the responsibilities of several departments.

The Diversified Operations Group is now better equipped to assist the more recently acquired subsidiaries. Innovation and new undertakings have been the order of the day for United Cigar Stores, Canada Foils, Growers' Wine Company and Beau Chatel Wines.

The quest for new undertakings has been more sharply defined, and separated from other operations of Imperial Tobacco, by the formation of Innotron International Limited with a separate staff and separate offices, and incorporation in the United States as well as Canada.

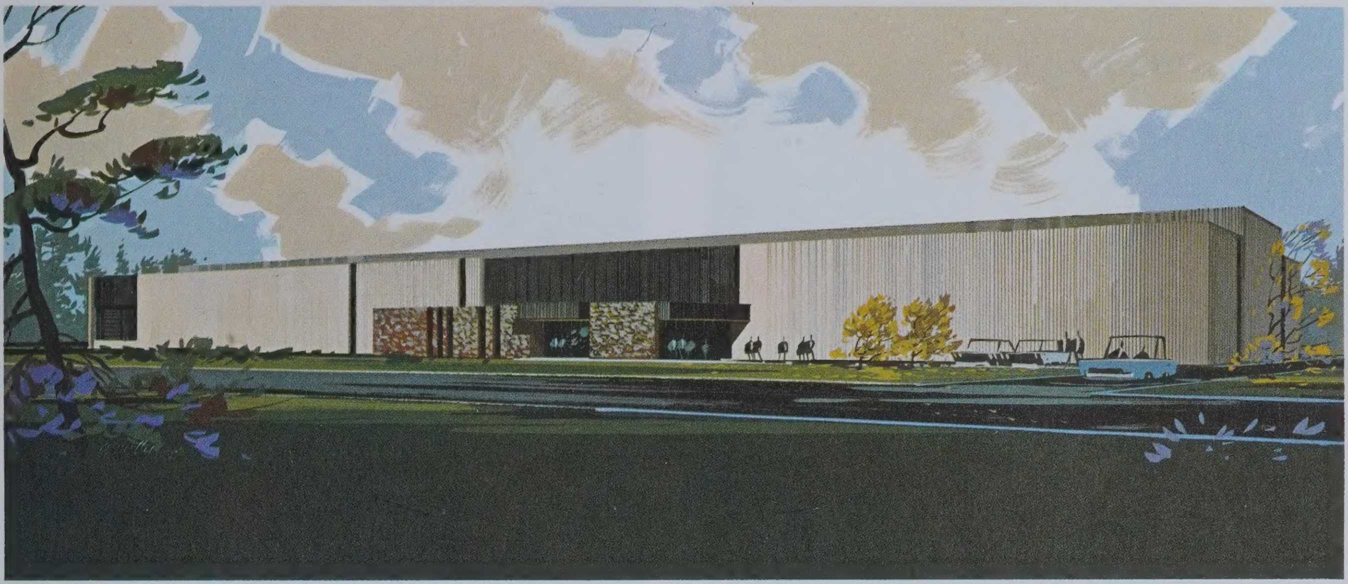
Working to the defined objective of "new acquisitions and marketing innovation", many of the youthful Innotron group are completely freed of other corporate responsibilities. The emphasis on innovation has already been applied within Imperial Tobacco's sphere of activities on the principle that, "to survive and to grow, the corporation must innovate."

As one financial publication recently described Innotron, "When the first big steps in diversification appear, they will be as measured, as considered and as technically analysed as modern administrative technologies can make them."

To date more than 100 companies have been examined and scored on a specific set of criteria. The investigation

Premier Alex Campbell of Prince Edward Island, left, joined D. E. Kearney (right), vice-president, leaf operations, and Robert J. Lovell, resident manager of leaf operations in the Maritimes, in announcing Imperial Tobacco's purchase of four farms and the launching of a program to assist present and prospective growers.

This architect's drawing shows the $7,000,000 aluminum strip casting mill being built at Bracebridge, Ontario, by Canada Foils, Limited, an Imperial Tobacco subsidiary, to supply materials for its foil and flexible packaging manufacturing operations in Toronto.



of investment and development possibilities has been narrowed down to the point where at least one significant acquisition will probably be completed later this year.

As a separate activity, Imperial Tobacco is entering the field of closed-circuit television through the acquisition of Simtel Incorporated, a small Montreal-based company providing creative services and equipment for closed-circuit programs in industry.

The potential of this vital new vehicle of communication is just beginning to be tapped and may possibly be accelerated by the added skills and resources which the Company brings to bear.

Convinced of the value and impact of information being conveyed to staff this way, Imperial Tobacco is introducing closed-circuit television to link its own principal offices and plants across the country on a regular basis.

CLIMATE OF CHALLENGE

To meet the rush of change all about us, the Company has concentrated on making jobs as challenging and satisfying as possible to employees at all levels. In the extensive program of upgrading machinery in the plants in Guelph, Quebec City and Montreal, which will be completed during 1968, the need for more skilled attention is being met through retraining our own employees. The program is so successful to date that all the new skills required are being supplied from our own present labor force.

This type of consideration for our employees resulted in jobs being available in the Guelph plant to every employee who wished a transfer from the 75-year-old Hamilton plant as its operations were phased out during the year. To resolve the problems of dislocation of employment, each employee, whether transferring or remaining in Hamilton, received individual attention. The Company's policy and procedures attracted widespread interest and favorable comment.

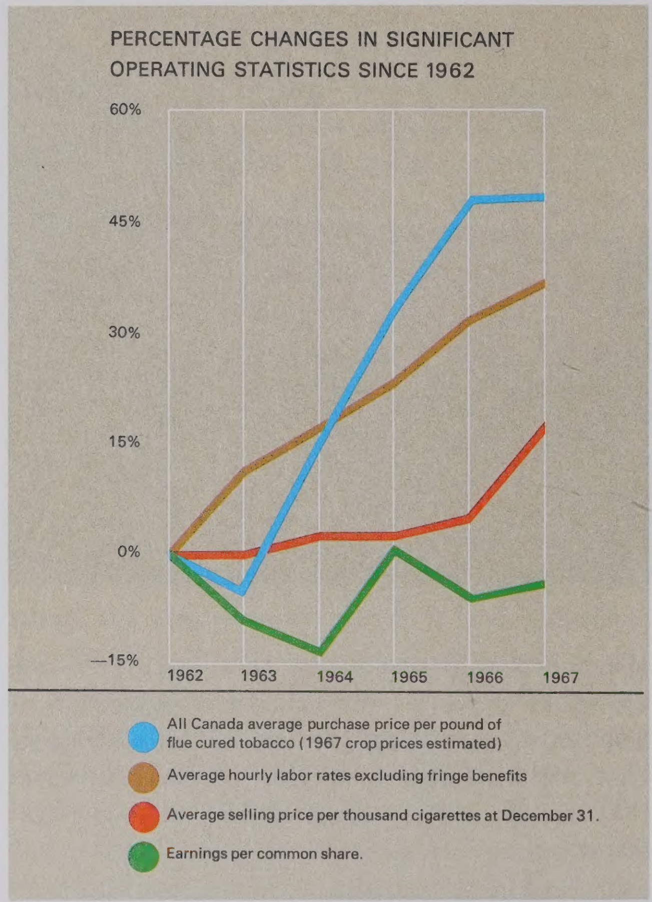
INVENTION AT WORK

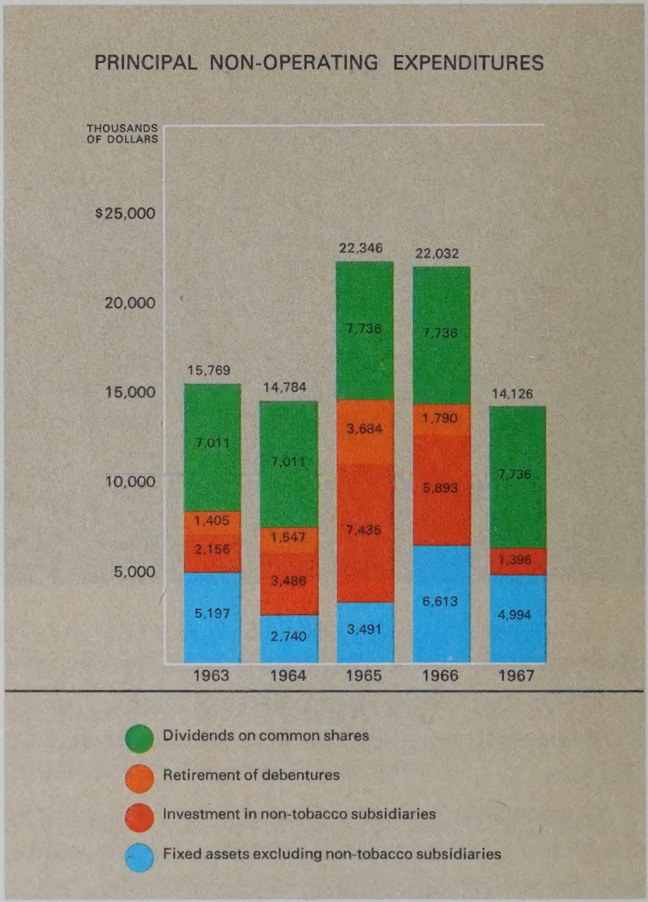
In the field of engineering, long a Company strength, a new automatic weighing and classifying device was developed for fine cut tobaccos. This breakthrough permits more accurate weighing with more uniform strand length, an important quality improvement for smokers of fine cut tobaccos.

A new automatic feeding system for cigarette making machines is being developed which will provide more uniformly-filled cigarettes and can be adapted to groups of machines operating at the same time.

The Company's engineers, in their continuous search for improved materials and methods, have used a new metallic wall facing for the Quebec City plant. This enamel-covered steel siding is expected to last longer, require less maintenance and result in improved appearance over any siding used in the past.

The far-ranging activities of the engineering department have included an attack on the problem of hijacking of trucks laden with large cigarette shipments. By filming special serial numbers and registering shipments, a record is made of each truck shipment. The availability of this record helped crack a recent case of hijacking. The hijackers were apprehended by the police, who also recovered the shipment. Faced with irrefutable evidence, the five hijackers have all pleaded guilty.





HOW THE SCIENTIST SUPPORTS MARKETING

The new and larger home for research and development has made possible more intensive and extensive activities.

Among accomplishments last year, a more effective and uniform method of mentholating cigarettes was introduced.

Another achievement came from a technical problem in the marketing of cigars. The *Old Port* cigarillo had become popular, but the trend toward tipped cigarillos suggested that this variety should also be available. However, how could the unique *Old Port* flavor reach the smoker through a polyethylene tip?

Working with the suppliers and the moulders, Imperial Tobacco's scientists developed a method of applying just the right flavor to the tip itself that did not break down in the high temperatures of the moulding process. The resulting *Old Port* tipped cigarillo was soon in greater demand than could be supplied. The new product has aroused widespread interest in other countries to the point that licensing arrangements are being prepared.

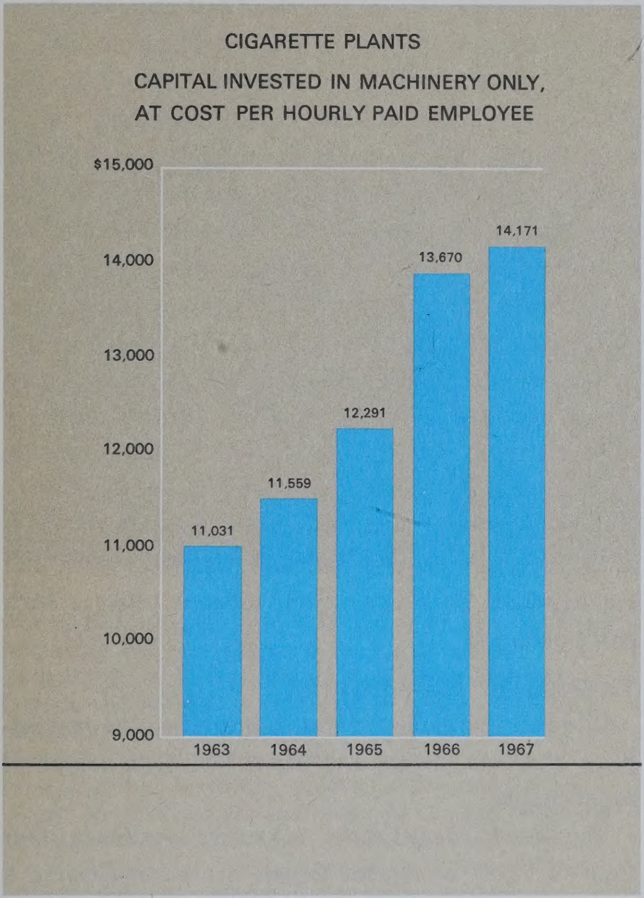
In a continuous effort to satisfy the needs of the market-place, the research and development staff engage in a constant assessment of tobacco blends, filters, packaging and processing methods to establish desired taste, firmness, draw resistance and other attributes.

During the past year, the laboratory has acquired new equipment for analysing tobacco and smoke and for evaluating wrapping materials. For example, several units simulate extreme ranges of climatic and humidity conditions. The effects of these extremes are tested on tobacco and wrapping materials. As one instance, a cycle of warm dry conditions and warm humid conditions will show the extent of distortion of packages, if any, caused by cellophane shrinkage.

THE STRICKMAN FILTER

When the Strickman filter was announced last July, Imperial Tobacco scientists went to the inventor's laboratories in Hillsdale, New Jersey, to test the filter's performance. Since that meeting, there have been frequent exchanges at the scientific level.

Because the Strickman filter is a polymer compound in powder form, different from conventional fibre filters, new techniques of manufacture and assembly will have to be developed. As soon as Imperial Tobacco has been licensed to use the filter, the Company will expedite the



Far left
With costs continuing to rise, price increases in longer length cigarettes were introduced late in 1967. Imperial Tobacco earnings improved during the year.

Centre
The difference in non-operating expenditures in 1967 from 1966 was largely due to the smaller amount of new investment in subsidiaries. Dividends last year were the same as the previous year.

Right
Investment per employee in machinery has continued to climb each year, reflecting the constant quest for improved productivity.

many stages of testing and development in order to offer cigarettes with the new filter to Canadian smokers.

LEAF TOBACCO PRICES

The cost structure of the tobacco manufacturer depends heavily on tobacco growers. Prices for the 1967 crop of leaf tobacco averaged about the same as the previous year, which had been at an all-time high. During this season's auction, neither domestic nor overseas manufacturers were able to buy enough tobacco to meet their complete needs because of a shortage in the flue-cured leaf tobacco crop in southern Ontario.

Acreage had been allotted realistically by the Marketing Board last year to yield the estimated requirement of 238,000,000 pounds of flue-cured tobacco, but excessively wet weather early in the season seriously cut the crop. It is hoped the acreage of tobacco planted this spring will provide for all domestic needs, as well as an ample supply for overseas shipments which are important to Canada's foreign trade.

FARMS BOUGHT IN P.E.I.

As a step toward encouraging farmers to grow tobacco as a cash crop in Prince Edward Island, the Company purchased four farms totalling 425 acres in

Some 50 members of the Toronto Society of Financial Analysts visited Imperial Tobacco's Guelph plant in July, inspected the modern manufacturing operations, and engaged in a two-hour discussion with company officers on financial and management matters.

the Glen Martin area of the Island last year. One farm is being equipped to grow cigarette leaf during 1968.

This operation will be modelled on that of Imperial Tobacco's South Middleton, Ontario, practical experimental farm, where new developments in equipment and growing practices are tested and evaluated. Company specialists have been working with farmers and provincial agronomists in P.E.I. for some years, and in 1967 cigarette leaf was grown on 519 acres on 18 farms.

The Company has maintained a policy of giving help to areas where farmers have wanted to produce tobacco in any province of Canada that has shown reasonably promising soil and climatic conditions. Much land in Prince Edward Island not presently being farmed appears suitable should farmers be prepared to invest in the specialized equipment, skills and hard work that are required. As a cash crop, tobacco offers a high profit potential.

TRENDS IN CIGARETTES

Competition among cigarette brands in the marketplace has been intense and has reflected the tempo of rapid change.

The trend toward filter cigarettes continues. Our *Player's Filter* in regular length has been showing a steady upward trend while such well-established brand names as *du Maurier*, *Peter Jackson* and *Matinée* hold important shares of the filter market. In plain ends, *Player's* is the leading brand.

While king size cigarettes have been gaining in popularity, the regular length cigarettes still account for more than half of all cigarettes sold. The Company's leading brands are again *du Maurier*, *Peter Jackson*, *Player's* and *Matinée*.

The menthol cigarette market in Canada has grown steadily in recent years with our *Cameo* continuing to be the dominant brand. A new *du Maurier* menthol cigarette has been introduced and should establish itself effectively during this year.

With the quick appeal shown for the extra-long cigarettes in the United States, the Company launched the *Goldcrest* brand, which was the first full 100 millimetre brand developed specially for the Canadian market.

PROMOTIONS BRING WORLD STATURE

The marketing division engaged in a wide variety of promotional activities during the year. Among the most effective of these has been the linking of brand names with major sporting competitions of national and international status.

The Right Honorable Roland Michener, Governor-General of Canada, and Mrs. Michener graciously received company officers and the three grand prize winners of Canada — 2000 A.D. *at Government House in Ottawa on the last Friday of Centennial Year, presenting illuminated scrolls to the winners.*
From left: John M. Keith, president of Imperial Tobacco; winner James Willer of Vancouver; the Governor-General; Mrs. Michener; winner Prof. Clément Moisan of Laval University, Quebec City; and winner Prof. Perry Meyer of McGill University, Montreal. For further details, please see page 15.

The *Player's* family of brands has for several years provided major support to the development of sports car racing by providing trophies, prize money, advertising and publicity at key events across Canada. Largely through these efforts Canada has gained world recognition so that, during Centennial year, *Player's* sponsored Canada's first international Grand Prix automobile race at Mosport, Ontario. Points earned by drivers were counted into their totals for the world driving championship.

Meanwhile, *du Maurier* in 1966 sponsored its first international-calibre ski competition in Canada and in 1967 the event again attracted famous skiers from many nations. Last year Canada's own Nancy Greene gave up her entry in three European events to come home and compete in the *du Maurier International*, winning top women's honors. This year world status has been accorded Canada with points won in the *du Maurier International* counting toward the coveted World Cup.

ADVANCE IN CIGAR SALES

General Cigar Company, Limited, the cigar manufacturing subsidiary of Imperial Tobacco, recorded a 12 per cent jump in sales. The *Old Port* family of brands continued in its leading position, accounting for one of every four cigars sold in Canada.

The *Old Port* tipped cigarillo could not be manufactured fast enough to meet the demand. The program for national distribution was extended to most provinces in 1967 and will be completed during the early part of this year. A newly-developed machine purchased by the Company makes possible a great increase in output.

The re-designed *White Owl* packaging was enhanced by the beauty of a painting of the owl by the noted Canadian artist Fenwick Lansdowne of Victoria, B.C. Permission was also secured to use 24 of his paintings of Canadian birds, which have been attractively reproduced on cards, with one card inserted in each package of *White Owl* cigars.

The use of silver and gold metallized cellulose film on the *Reas* cigars represented a world first and doubtless contributed to the upward spurt in sales of the brand.

The development of cigar sales to other countries assumed greater importance with an increase of 50 per cent last year and a further sizeable jump projected for 1968. Australia is the largest importer at present but others include Honduras, the West Indies, Libya and Hong Kong. Recently a large order was received from Japan for the first time.

Among pipe tobaccos the new half-pound tin of *Old Port* attracted attention and is selling well. *Hollandia* and *Old Chum* continue to be popular with pipe smokers as does our new *Matinée* fine cut for those who roll their own cigarettes.

A surprisingly large volume of snuff is sold in Canada, primarily for use by workers in mines and oil refineries. *Copenhagen* snuff is now being packaged in a new vacuum can, an innovation that ensures freshness for a long period of time and thus contributes to improved manufacturing efficiency.

PROGRESS BY NON-TOBACCO SUBSIDIARIES

Vigorous activity was particularly evident last year in Imperial Tobacco's subsidiary companies. Each has been busily engaged in organizing itself for broader horizons.

Plans for a significant capital investment of $7,000,000 in a new plant were announced by Canada Foils, Limited. Construction was begun in late 1967 on an aluminum strip casting mill at Bracebridge, Ontario, which will supply material to Canada Foils' Toronto plant for use in its production of foil and flexible packaging.

The new plant will produce aluminum strip from ingots by a patented process for which Canada Foils is exclusive licencee in Canada. The plant is being built on a 52-acre site, and will initially provide 50,000 square feet of manufacturing space. The design and construction of this facility allow for future expansion.

Canada Foils has been broadening its base of products in different ways. By opening a small plant in Montreal, it is better able to serve Quebec customers and has installed special equipment that combines die-cutting, printing and forming to turn out a range of high quality labels and small cartons.

The Toronto plant is the first in Canada to install vacuum metallizing equipment to supply the ever-widening market for metallized film, first developed for space suits. Previously this material was imported from the United States.

Although suffering growth problems, Castle Wines, operated by Growers' Wine Company Limited of British Columbia, met expectations in increased sales volume for 1967. The prestige *Ste. Michelle* table wines sold rapidly. More listings were obtained in the western provinces, with wider distribution from the winery in British Columbia and from the new winery in Moose Jaw, Saskatchewan, where sales were ahead of forecast.

During the year, Beau Chatel Wines Limited in Ontario introduced *Light n' Easy* Sparkling Cider, a carbonated drink containing 6.9 per cent alcohol by volume and designed to appeal to light, modern tastes. Advertising for this new product marked the first use of TV as an advertising medium by a Canadian winery. The product has been well received.

Before Christmas, Beau Chatel introduced three new table wines, *St. Maurice* white extra dry and medium dry, and *Vino Buono* red.

The wine business in the province of Ontario is exceedingly competitive and presents a demanding challenge to gain a satisfactory share of market.

United Cigar Stores, with more than 250 outlets across Canada, has long been a subsidiary of Imperial Tobacco. The proportion of its "product mix" has been changing from concentration on tobacco products and accessories to inclusion of a wider variety of other lines.

A possible new trend is represented in the opening of the stylish *Inclination* stores in the Toronto-Dominion Centre in Toronto and Place Bonaventure in Montreal. Other approaches to a distinct — and distinguished — shopping character are *Le Fumeur* in Place Ville Marie in Montreal, and *Men of York* in the Toronto-Dominion Centre.

OTHER RESPONSIBILITIES

Among the Company's interests, the new distributive policy for jobbers, established in 1965, has developed a new confidence in the distributive trades and contributed toward a more effective and efficient system.

The tobacco industry in Canada has continued its active concern in questions of smoking and health and representatives of the *ad hoc* committee of the industry serve as members of the Technical Advisory Committee established by the federal Department of National Health and Welfare.

Imperial Tobacco has been working with inventor Robert Strickman since last August to explore possibilities for use of the Strickman filter on the Company's cigarettes. At top, Dr. Victor Runeckles (left), manager, research laboratory, shows Mr. Strickman the new facilities of the Company's enlarged research centre opened last year.

Centre: During a special "open house" for employees at the centre, a technician shows her visitor the stretch and breaking tests carried out on samples of cigar tobacco.

Below: Two visitors are obviously intrigued as a technician explains how a distillation column produces an extract from a tobacco sample for further testing.


Player's
"PLAIN"
OLD CHUM
PIPE TOBACCO
REAS
All Havana
Belvedere
LIGHT CANDELLA
REAS
All Havana
Petit
Corona
LIGHT CANDELLA
AROMATIC
Hollandia
REGULAR
Hollandia
REAS
All
Havana
Corona
Grandes
ENGLISH MARKET
SELECTION
REAS
All Havana
Belvedere
ENGLISH MARKET SELECTION
REAS
All Havana
Petit
Corona
ENGLISH MARKET SELECTION
du MAURIER
du MAURIER
Matinée
KINGS
Matinée
CAMEO


Player's
FILTER
Player's
CIGARETTE
TOBACCO
CHOICE VIRGINIA
Matinée
TABAC A
CIGARETTES
Embassy
TABAC A
CIGARETTES
VOGUE
CIGARETTE
TOBACCO
MILD
House of Lords
PETIT CORONAS
25
white owl
white owl
KING SIZE
Peter Jackson
white owl
white owl
GOLDCREST
W.D. & H.O. Wills

A "new look" is coming to United Cigar Stores with the opening of new retail outlets in major shopping plazas. Men of York, *at left, and* Inclination, *right, are both located in the shopping plaza of the Toronto-Dominion Centre office development in downtown Toronto. Another* Inclination *is in Montreal's Place Bonaventure shopping centre and merchandise mart, while* Le Fumeur *in Montreal's Place Ville Marie has distinctive decor as does* Men of York. *Shareholders living in or visiting Toronto and Montreal are invited to see their wide range of gift items, smoking supplies, and other merchandise.*

EMPLOYEE EDUCATION

In addition to the training activities mentioned earlier, the Company is continuing its efforts to provide a complete educational program for employees. This year Imperial Tobacco offered a "continuing education program" which enables employees in the Montreal, Granby, Quebec City, and Guelph plants to take further secondary school courses.

The program has the support of the Departments of Education of Quebec and Ontario, which pay the salaries of teachers whose services are obtained through local school boards. In most plants, the Company provides in-plant classrooms and text books. Classes are organized wherever 20 or more "students" ask for a given subject.

COMMUNITY SUPPORT

In educational and community activities, many employees participate enthusiastically and the Company offers tangible support wherever practical. One example of an activity that may yield a potentially important result is a special two year grant by Imperial Tobacco to the School of Business of the University of Toronto for a research study on the use of management development techniques to facilitate organizational changes.

The Company supported significant musical events in Winnipeg, Calgary, Edmonton and Vancouver along with other community endeavors in many cities across Canada. We derived particular satisfaction from our Centennial project, *Canada — 2000 A.D.* This idea competition on the future of Canada attracted more than 1,000 entrants from whom ten finalists were chosen. Each of the finalists won $3,000 and was required to

submit a book-length manuscript to compete for the Grand Award. All ten made their submissions by the deadline of September 1, 1967 and the panel of judges announced its decision at the end of October that the Grand Award of $30,000 be shared equally among three of the finalists.

Private presentation ceremonies were held in Toronto and Quebec City and the grand culmination, as portrayed on page 9 of this report, took place in Government House in Ottawa on December 29 when His Excellency the Right Honorable Roland Michener, Governor-General of Canada, and Mrs. Michener received the three winners and their families and presented special Scrolls of Recognition.

Efforts to keep employees and interested segments of the public informed about the Company's activities showed a marked increase. Many invitations for public speaking engagements and press, radio and television interviews were accepted by officers and senior members of the staff.

A field trip was organized for Toronto financial analysts to visit the Guelph plant, during which a two-hour discussion session was held with a number of Company officials, as shown on page 8 of this report.

During the year awards were received for the Company's 1966 Annual Report and for the monthly employee publication, "The Leaflet/Le Feuillet". The Annual Report placed second in its industry category for all North America in the competition sponsored by the Financial World publication of New York City. The employee publication won a certificate of merit from the Canadian Industrial Editors Association.

Changes in the Board of Directors during the year included the additions of Peter R. Austin and Henri W. Joly. Retiring from the Board were J. A. Calder, previously an executive vice-president; R. B. B. Lansdown, vice-president, manufacturing; and A. Reid Tilley, vice-president, corporate planning. All three had been with the Company for many years and made important contributions to its progress.

The problems for any business today and the fiercely competitive conditions of the tobacco industry place great demands on all our employees. The Board of Directors appreciates the enthusiasm and conscientious efforts shown by our employees in all operations of Imperial Tobacco and its subsidiary companies.

For the year now well launched we are forecasting a modest increase in the sale of tobacco products, improvement in the progress of our subsidiaries, and a possible increase in earnings.

On behalf of the Board of Directors,

John M. Keith

President

Montreal, 16th February 1968.

DIRECTORS:

PETER R. AUSTIN
WILLIAM H. BOOTH
BERNARD DANSEREAU, Q.C.
T. E. R. HAWKINS
HENRI W. JOLY
D. EDWARD KEARNEY
JOHN M. KEITH
LEO C. LAPORTE
PAUL PARÉ

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JOHN M. KEITH, *president*
PAUL PARÉ, *executive vice-president*
WILLIAM H. BOOTH, *vice-president*
T. E. R. HAWKINS, *vice-president*
D. EDWARD KEARNEY, *vice-president*
LEO C. LAPORTE, *vice-president*
BERNARD DANSEREAU, Q.C., *general counsel and secretary*
MATTHEWS GLEZOS, *treasurer*
R. A. HILLHOUSE, *comptroller*
GEORGE G. ROSS, *comptroller*
PIERRE ROBERGE, *assistant secretary*

DELOITTE, PLENDER, HASKINS & SELLS, *auditors*
TOUCHE, ROSS, BAILEY & SMART, *accounting consultants*

Transfer Agents
Crown Trust Company, Montreal
The Royal Trust Company, Halifax, Toronto, Vancouver

Registrars
Montreal Trust Company, Halifax
National Trust Company, Limited, Montreal, Toronto, Vancouver

Stock Exchange Listings
Montreal, Toronto, Vancouver and London, England

COMMENTS ON THE YEAR'S OPERATIONS

Beau Chatel Wines Limited, a wholly-owned subsidiary, has been included in the 1967 consolidated financial statements for the first time. For comparative purposes the 1966 figures have been restated to reflect the accounts as they would have appeared for the 1966 year had Beau Chatel Wines Limited been included. The consolidated financial statements now include the accounts of all wholly-owned subsidiaries but exclude the non-wholly-owned subsidiaries of Canada Foils, Limited and Growers' Wine Company Limited. It is our intention to consolidate the accounts of all subsidiaries sometime in the future. If partially-owned subsidiaries were to adopt replacement cost accounting, the rights and interests of certain classes of minority shareholders might be affected. As the practical problems of replacement cost accounting are bound to increase when further acquisitions are made, it has been decided to review the merits of the system and a re-assessment of its value will be made.

CONSOLIDATED EARNINGS

Consolidated net sales of $393,315,000 were the highest sales ever reported in the history of the company. They showed an increase of $20,246,000, or 5.4% over 1966. However, as 1967 was another year characterized by increasing costs, earnings from operations rose by only $894,000, or 4.1%.

Income from investments in non-consolidated subsidiaries declined from $336,000 to $149,000. However, as shown below, these companies made considerable progress during 1967:

	Canada Foils, Limited		Growers' Wine Co. Ltd.	
	1967	1966	1967	1966
Sales	$10,977,000	$9,221,000	$3,895,000	$3,452,000
Net Earnings	278,000	216,000	106,000	21,000
Imperial Tobacco Portion of Earnings	277,000	215,000	58,000	11,000
Dividends received	142,000	274,000	7,000	62,000

Consolidated net earnings at $12,741,000, were up by $279,000 over 1966, an increase of 2.2%. After preference share dividends, earnings per common share were $1.28, up from $1.25 on the adjusted 1966 basis. Had Beau Chatel Wines Limited been excluded from consolidation again this year, then earnings per common share for 1967 would have been $1.30 compared to $1.28 reported last year on a like basis.

CONSOLIDATED RETAINED EARNINGS

A transfer of $276,000, being excess depreciation no longer required, was made from accumulated depreciation to retained earnings. A charge of $439,000 resulted from the loss on sale of fixed assets and the capital increment of $2,186,000 applicable to those assets was transferred to retained earnings.

During the year 111,942 of the 6% cumulative preference shares were purchased and cancelled. The premium, brokerage and tax on these shares, amounting to $138,000, was charged to retained earnings, and $545,000 representing the par value of the cancelled shares, was transferred to capital surplus.

During 1966 Beau Chatel Wines Limited wrote off $80,000 of goodwill, which was included in their accounts at the time of acquisition. On consolidation of Beau Chatel Wines Limited, goodwill amounted to $233,000 which was written off against retained earnings in 1967.

Regular dividends were paid during the year on outstanding 6% cumulative preference shares. A final dividend of 10 cents per share has been declared payable 29th March 1968, making total dividends of 80 cents per common share, the same as was paid for last year.

Net earnings exceeded dividends by $4,639,000, which together with the adjustments referred to above resulted in an increase in consolidated retained earnings of $5,746,000.

BALANCE SHEET

Working capital increased by $2,743,000 as explained in detail in the statement of changes in consolidated working capital on page 24. The main changes occurred in inventory which increased by $6,838,000, the major part of which was in leaf stocks; and in income, excise and other taxes which increased by $5,169,000, largely due to increased excise tax on tobacco products which came into effect 1st December, 1967.

Fixed assets were revalued at 31st December 1967, and, in spite of 1967 being a year of inflation, the capital increment decreased by $2,334,000. Of this amount $2,186,000 is accounted for by the removal of the increment applicable to disposals and $148,000 due to the net change in replacement values. Although the basic replacement cost increased, this was offset by a reduction in the replacement cost of machinery imported from the United Kingdom due to the devaluation of sterling, coupled with the removal of sales tax on production machinery which was taken into account in computing replacement costs. The reduction in replacement cost gave rise to the excess depreciation referred to in the retained earnings section.

GENERAL

Toward the end of the year it became increasingly clear that increased costs would have to be reflected in a price increase. It was with reluctance that selective price increases in the longer length cigarettes were announced on 28th November 1967 to become effective on 6th December. No change was made in the price of regular size cigarettes. The new prices were more in line with the production costs of each category. On 30th November the government announced increases in excise tax applicable to tobacco products. The increase in excise tax was added to our new cigarette prices and price adjustments were made for other products to include the increased tax. Coming as they did late in the year, the combined effect of increased prices and tax was minimal on total sales and earnings in 1967.

Following declaration of the final dividend on common shares for 1967, the first interim for 1968 of 17½ cents per share was declared payable 29th March 1968.

IMPERIAL TOBACCO COMPANY OF CANADA LIMITED and Subsidiary Companies
Year ended 31st December 1967 with comparative figures for 1966*

CONSOLIDATED EARNINGS (note 1)

	1967	1966*
Net sales	$393,315,000	$373,069,000
Federal sales and excise taxes and excise duty	216,845,000	212,434,000
Manufacturing costs, merchandising and general expenses (note 2)	148,650,000	133,879,000
Depreciation (note 3)	5,034,000	4,864,000
Total cost of operations	370,529,000	351,177,000
Earnings from operations	22,786,000	21,892,000
Income from investments in non-consolidated subsidiaries (note 1)	149,000	336,000
Income from other investments	1,466,000	1,631,000
	24,401,000	23,859,000
Interest on funded debt	68,000	83,000
Earnings before income taxes	24,333,000	23,776,000
Income taxes	11,592,000	11,314,000
Net earnings for the year	$ 12,741,000	$ 12,462,000

CONSOLIDATED RETAINED EARNINGS (note 1)

	1967	1966*
Retained earnings 1st January	$ 51,305,000	$ 47,882,000
Decrease in retained earnings of Beau Chatel Wines Limited from date of acquisition to 1st January 1966	—	39,000
	51,305,000	47,843,000
Net earnings for the year	12,741,000	12,462,000
Excess depreciation no longer required (note 3)	276,000	(749,000)
Net loss on disposal of fixed assets	(439,000)	(300,000)
Capital increment applicable to disposal of fixed assets	2,186,000	575,000
Premium, brokerage and tax on 6% cumulative preference shares purchased	(138,000)	(68,000)
Transferred to capital surplus (note 7)	(545,000)	(248,000)
Write-off of goodwill	(233,000)	(80,000)
	65,153,000	59,435,000
Dividends (note 4)	8,102,000	8,130,000
Retained earnings 31st December	$ 57,051,000	$ 51,305,000

*For comparative purposes 1966 figures have been revised in accordance with the 1967 presentation (note 1).
The notes on pages 19 and 20 form an integral part of these statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. *Principles of consolidation and related information*

The consolidated financial statements include the accounts of Imperial Tobacco Company of Canada Limited and all wholly-owned subsidiaries, including Beau Chatel Wines Limited for the first time. For comparative purposes the 1966 figures have been restated to reflect the accounts as they would have appeared for the 1966 year had Beau Chatel Wines Limited been included. It is considered impractical at this time to consolidate Canada Foils, Limited and Growers' Wine Company Limited, which are not wholly owned.

The earnings of non-consolidated subsidiaries have been included in the consolidated accounts only to the extent of dividends received.

In respect of non-consolidated subsidiaries, the company's proportion of (a) the net earnings for the year ended 31st December 1967 amounted to $335,000 and (b) the net increase in retained earnings since acquisition to 31st December 1967 amounted to $347,000.

2. *Manufacturing costs, merchandising and general expenses*

Included in this item is the amount of $507,000 (1966 — $513,000) for total remuneration paid to directors, all of whom were full time officers or employees of the company. In addition $77,000 (1966 — $58,000) was paid for total remuneration to senior officers who were not directors of the company.

3. *Fixed assets and depreciation*

a) Depreciation charged against earnings for the year and accumulated depreciation to date are based on replacement cost both in the consolidated statements and in the books of the individual companies. The same rates applied to historic costs would have given rise to a charge for the year of $4,135,000 (1966 — $3,835,000) and accumulated to date of $39,198,000 (1966 — $37,017,000).

b) Reduced depreciation requirement of $276,000 in respect of prior years, arising from current year's decrease in replacement cost, has been transferred to retained earnings (1966 — $749,000 additional requirement transferred from retained earnings).

c) Fixed assets are recorded in the books of the companies at historic cost and are shown at replacement cost only on consolidation.

d) The replacement cost of fixed assets is based on appraisals made as at 31st December. For 1967, buildings were appraised at replacement cost and land at current market value by Canadian Appraisal Company Limited. Machinery and equipment were valued at replacement cost by company officials utilizing price indexes obtained from the Dominion Bureau of Statistics and, where necessary, price indexes based on government and industry studies in other countries. On consolidation the use of replacement cost gives rise to an increase in fixed assets before depreciation of $37,383,000 (1966 — $39,717,000) which is reflected in capital increment.

e) The effects of the foregoing are summarized as follows:

	1967	*1966**
Land, buildings and equipment at historic cost	$ 78,044,000	$ 75,215,000
Capital increment	37,383,000	39,717,000
Replacement cost	115,427,000	114,932,000
Less:		
Accumulated depreciation 1st January	66,371,000	61,926,000
Accumulated depreciation on disposals during year	(3,695,000)	(1,168,000)
Depreciation for the year	5,034,000	4,864,000
Excess depreciation no longer required and transferred to retained earnings (1966 — the reverse)	(276,000)	749,000
Accumulated depreciation based on replacement cost	67,434,000	66,371,000
Fixed assets	$ 47,993,000	$ 48,561,000

1967	*1966**
$ 10,182,000	$ 11,559,000
13,303,000	11,835,000
17,044,000	16,509,000
82,608,000	75,770,000
123,137,000	115,673,000
9,521,000	9,961,000
22,896,000	17,727,000
1,057,000	1,065,000
33,474,000	28,753,000
89,663,000	86,920,000
2,503,000	1,251,000
12,318,000	12,174,000
1,021,000	951,000
359,000	540,000
1,345,000	1,225,000
47,993,000	48,561,000
1,000	234,000
155,203,000	151,856,000
2,261,000	2,261,000
2,125,000	2,190,000
4,386,000	4,451,000
$150,817,000	$147,405,000
54,326,000	54,871,000
37,383,000	39,717,000
2,057,000	1,512,000
57,051,000	51,305,000
$150,817,000	$147,405,000

Approved by the Board:
JOHN M. KEITH, Director
W. H. BOOTH, Director

CONSOLIDATED EARN

Net sales...

Federal sales and excise taxes and
Manufacturing costs, merchandisin
Depreciation (note 3)...
Total cost of operations...

Earnings from operations...
Income from investments in non-cc
Income from other investments...

Interest on funded debt...
Earnings before income taxes...
Income taxes...
Net earnings for the year...

CONSOLIDATED RETA

Retained earnings 1st January...
Decrease in retained earnings of Be
from date of acquisition to 1st .

Net earnings for the year...
Excess depreciation no longer requ
Net loss on disposal of fixed assets.
Capital increment applicable to dis
Premium, brokerage and tax on 6%
Transferred to capital surplus (note
Write-off of goodwill...

Dividends (note 4)...
Retained earnings 31st December...

*For comparative purposes 1966 figur
The notes on pages 19 and 20 form ar

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. *Dividends*

Dividends of Imperial Tobacco Company of Canada Limited:

	1967	*1966*
On 6% cumulative preference shares	$ 366,000	$ 394,000
On common shares:		
Four interim dividends totalling 70 cents per share	6,769,000	6,769,000
Provision for final dividend for year of 10 cents per share	967,000	967,000
	$ 8,102,000	$ 8,130,000

5. *Provision for dividends*

Provision for dividends of Imperial Tobacco Company of Canada Limited:

	1967	*1966*
Accrued on preference shares	$ 90,000	$ 98,000
Final for year on common shares	967,000	967,000
	$ 1,057,000	$ 1,065,000

6. *Paid up share capital*

		1967	*1966*
6% cumulative preference shares par value $4.86⅔ each			
Authorized and issued	1,650,000 shares		
Less purchased and cancelled:			
as at 31st December 1966	310,665 shares		
	1,339,335 shares		$ 6,518,000
during 1967	111,942 shares		
Outstanding 31st December 1967	1,227,393 shares	$ 5,973,000	
Redeemable sinking fund preference shares par value $25 each			
Authorized: 200,000 shares			
Issued: None		—	—
Common shares no par value			
Authorized: 10,800,000 shares			
Issued: 9,670,532 shares		48,353,000	48,353,000
		$ 54,326,000	$ 54,871,000

7. *Capital surplus*

The sum of $545,000 (1966 — $248,000) has been transferred from retained earnings and designated as capital surplus arising from cancellation of 111,942 (1966 — 51,038) 6% cumulative preference shares par value $4.86⅔ each.

8. *Pension and retirement plans*

Outstanding commitments in respect of funding of back service of employees under a trusteed pension plan amount to $3,835,000 at 31st December 1967 (1966 — $4,225,000) payable in annual instalments to 1981. The 1967 instalment was $390,000 (1966 — $390,000).

There is an estimated liability of $2,669,000 in respect of various unfunded retirement allowances. Current payments under these plans, as in the past, have been charged against current operations.

CONSOLIDATED BALANCE SHEET (note 1)

	1967	1966*
CURRENT ASSETS		
Cash and term deposits	$ 10,182,000	$ 11,559,000
Marketable securities (market value $13,349,000; 1966—$11,907,000)	13,303,000	11,835,000
Accounts receivable less allowance for doubtful accounts	17,044,000	16,509,000
Leaf tobacco and other inventories (at average cost)	82,608,000	75,770,000
Total Current Assets	123,137,000	115,673,000
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	9,521,000	9,961,000
Income, excise and other taxes	22,896,000	17,727,000
Provision for dividends (note 5)	1,057,000	1,065,000
Total Current Liabilities	33,474,000	28,753,000
Working Capital (Net Current Assets)	89,663,000	86,920,000
OTHER ASSETS		
Loans and advances to non-consolidated subsidiaries	2,503,000	1,251,000
Investments in non-consolidated subsidiaries (at cost)	12,318,000	12,174,000
Other investments (at cost)	1,021,000	951,000
Special refundable tax	359,000	540,000
Prepaid expenses and deferred charges	1,345,000	1,225,000
Fixed assets (note 3)	47,993,000	48,561,000
Goodwill, trade marks and patents (at nominal value)	1,000	234,000
Excess of Assets over Current Liabilities	155,203,000	151,856,000
OTHER LIABILITIES		
3% sinking fund debentures (maturing 1st March 1970)	2,261,000	2,261,000
Accumulated income tax reductions applicable to future years	2,125,000	2,190,000
	4,386,000	4,451,000
Excess of Assets over Liabilities	$150,817,000	$147,405,000
Provided by:		
SHAREHOLDERS' RISK CAPITAL		
Paid up share capital (note 6)	54,326,000	54,871,000
Capital increment (note 3)	37,383,000	39,717,000
Capital surplus (note 7)	2,057,000	1,512,000
Retained earnings	57,051,000	51,305,000
	$150,817,000	$147,405,000

Approved by the Board:
JOHN M. KEITH, Director
W. H. BOOTH, Director

*For comparative purposes 1966 figures have been revised in accordance with the 1967 presentation (note 1).
The notes on pages 19 and 20 form an integral part of these statements.

STATISTICAL HIGHLIGHTS — TEN YEAR REVIEW

(Thousands of Dollars — except 'per common share' statistics)

	1967	1966(a)	1965	1964	1963
SALES AND EARNINGS					
Net sales (d)	393,315	373,069	366,262	351,456	355,065
Depreciation (e)	5,034	4,864	4,539	4,243	4,050
Earnings before income taxes	24,333	23,776	25,791	22,271	23,063
Income taxes	11,592	11,314	12,460	10,765	11,049
Net earnings	12,741	12,462	13,331	11,506	12,014
Earned on common shares	12,375	12,068	12,918	11,083	11,566
Per common share	$ 1.28	$ 1.25	$ 1.34	$ 1.15	$ 1.20
DIVIDEND RECORD					
On preference shares	366	394	413	423	448
On common shares	7,736	7,736	7,736	7,011	7,011
Per common share	$ .80	$ .80	$ .80	$ .72½	$ .72½
CAPITAL EXPENDITURES					
On fixed assets	5,187	8,451	3,491	2,740	5,197
FINANCIAL POSITION					
Current assets (f)	123,137	115,673	120,413	123,628	121,537
Current liabilities	33,474	28,753	32,992	30,024	28,120
Working capital	89,663	86,920	87,421	93,604	93,417
Investments in non-consolidated subsidiaries, including loans and advances	14,821	13,425	13,077	—	—
Fixed assets (before depreciation) (g)	115,427	114,932	105,962	99,510	97,688
Fixed assets (less depreciation) (h)	47,993	48,561	44,057	43,630	44,279
Debentures (i)	2,261	2,261	2,262	7,035	8,582
Excess of assets over liabilities	150,817	147,405	143,151	136,535	130,836
SHAREHOLDERS' RISK CAPITAL					
Equity of preference shareholders	5,973	6,518	6,766	6,973	7,215
Equity of common shareholders	144,844	140,887	136,385	129,562	123,621
Per common share	$14.98	$14.57	$14.10	$13.40	$12.78

(a) Revised to include Beau Chatel Wines Limited.
(b) 1960 revised in accordance with 1961 presentation.
(c) 1958/59 revised in accordance with 1961 presentation to the extent that equity reserves are included under shareholders' risk capital. Effect of replacement cost valuation of fixed assets on yearly charge for depreciation, on fixed assets, on accumulated depreciation and on equity of common shareholders and effect of write down on goodwill not reflected.
(d) Not published for years previous to 1960.

STATISTICAL HIGHLIGHTS — TEN YEAR REVIEW

(Thousands of Dollars — except 'per common share' statistics)

1962	1961	1960(b)	1959(c)	1958(c)	
					SALES AND EARNINGS
373,392	359,105	342,775	—	—	(d)......Net sales
3,757	3,482	3,402	4,332	3,871	(e)......Depreciation
25,594	26,800	26,177	24,222	21,481	......Earnings before income taxes
12,233	12,943	12,557	13,111	10,816	......Income taxes
13,361	13,857	13,620	11,111	10,665	......Net earnings
12,879	13,375	13,138	10,629	10,183	......Earned on common shares
$ 1.33	$ 1.38	$ 1.36	$ 1.10	$ 1.05	......Per common share
					DIVIDEND RECORD
482	482	482	482	482	......On preference shares
7,011	7,011	6,527	6,527	6,527	......On common shares
$ .72½	$ .72½	$ .67½	$ .67½	$ .67½	......Per common share
					CAPITAL EXPENDITURES
4,146	4,179	5,645	8,560	8,581	......On fixed assets
					FINANCIAL POSITION
123,127	117,590	112,503	108,487	105,731	(f)......Current assets
30,048	29,474	30,069	34,174	31,069	......Current liabilities
93,079	88,116	82,434	74,313	74,662	......Working capital
—	—	—	—	—	Investments in non-consolidated subsidiaries, ...including loans and advances
90,083	83,411	82,788	54,105	46,927	(g)......Fixed assets (before depreciation)
42,039	40,757	41,649	16,628	12,769	(h)......Fixed assets (less depreciation)
9,987	11,628	12,796	14,056	15,177	(i)......Debentures
125,842	118,058	111,456	108,963	104,135	......Excess of assets over liabilities
					SHAREHOLDERS' RISK CAPITAL
8,030	8,030	8,030	8,030	8,030	......Equity of preference shareholders
117,812	110,028	103,426	100,933	96,105	......Equity of common shareholders
$12.18	$11.38	$10.69	$10.44	$ 9.94	......Per common share

(e) 1960/67 based on replacement cost; 1958/59 based on historic cost and including charge for fixed asset replacement.

(f) 1960/62 revised to exclude prepaid expenses and deferred charges.

(g) 1960/67 based on replacement cost; 1958/59 based on historic cost.

(h) 1960/67 net after accumulated depreciation based on replacement cost; 1958/59 net after accumulated depreciation based on historic cost and including fixed asset replacement reserve.

(i) Excluding maturities within twelve months which are reflected in current liabilities.

STATEMENT OF CHANGES IN CONSOLIDATED WORKING CAPITAL
during the year ended 31st December 1967 with comparative figures for 1966*

	1967	*1966**
Increased by:		
Net earnings	$12,741,000	$12,462,000
Depreciation	5,034,000	4,864,000
Special refundable tax due within one year	344,000	—
Amount realized on sale of fixed assets	410,000	271,000
	18,529,000	17,597,000
Decreased by:		
Expenditures on fixed assets	5,187,000	8,451,000
Loans and advances to non-consolidated subsidiaries	1,252,000	1,251,000
Investments in non-consolidated subsidiaries	144,000	284,000
Other investments	70,000	(110,000)
Prepaid expenses and deferred charges	120,000	(57,000)
Special refundable tax	163,000	540,000
Dividends	8,102,000	8,130,000
Purchase of 6% cumulative preference shares	683,000	316,000
Debentures redeemed in advance of maturity	—	1,000
Accumulated income tax reductions applicable to future years	65,000	(704,000)
	15,786,000	18,102,000
Net increase (decrease)	2,743,000	(505,000)
Working capital at beginning of year	86,920,000	87,425,000
Working capital at end of year	$89,663,000	$86,920,000

*For comparative purposes 1966 figures have been revised in accordance with 1967 presentation (note 1).

AUDITORS' REPORT

DELOITTE, PLENDER, HASKINS & SELLS, Chartered Accountants
Sun Life Building, Montreal

To the Shareholders
of Imperial Tobacco Company of Canada Limited

We have examined the consolidated balance sheet of Imperial Tobacco Company of Canada Limited and Subsidiary Companies as at 31st December 1967 and the statements of consolidated earnings, consolidated retained earnings and changes in consolidated working capital for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances except that in the case of the non-consolidated subsidiary companies we have relied upon the reports of other auditors. Insofar as our opinion expressed below relates to information contained in the financial statements of those companies, it is based solely upon the reports of such other auditors.

In our opinion these financial statements, which incorporate the adjustment to the values of fixed assets referred to in note 3(c), present fairly the financial position of the companies as at 31st December 1967 and the results of their operations and changes in working capital for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

We also examined the statistical highlights which are presented as supplementary information and, in our opinion, this statement presents fairly the information shown therein.

Deloitte, Plender, Haskins & Sells
Auditors.

16th February 1968.

Printed in Canada


RAPIER
OLD PORT
RUM FLAVOURED WINE DIPPED
EXTRA MILD
OLD PORT
STRAIGHTS
CIGARILLOS
OLD PORT
EXTRA MILD
OLD PORT
CIGARILLOS
OLD PORT
PIPE TOBACCO
OLD PORT
PIPE TOBACCO
EXTRA MILD

TIME OF RAPID CHANGE

Our cover reflects the movement
and action of a busy street—
and the fast-paced world about us.